# Appendix B

## Tenet Healthcare Corporation Articles.

LOS ANGELES BUSINESS JOURNAL

October 8, 2001

# Reproductive Issues Surface in Tenet Takeover

BY LAURENCE DARMIENTO
*Staff Reporter*

When **Tenet Healthcare Corp.** sought to acquire Queen of Angels-Hollywood Presbyterian Medical Center three years ago little was said about Tenet's pledge to continue operating the facility under the moral teachings of the Catholic Church, which prohibit abortion, sterilization and other reproductive services.

But as the Santa Barbara-based company seeks to buy the Daniel Freeman hospitals in Marina del Rey and Inglewood, a women's group opposing the reproductive policy has caught the ear of the state Attorney General, which has regulatory authority over hospital sales. An official there called the issue one of the "red flags" raised by the prospective sale.

The California Women's Law Center wants Tenet to either provide reproductive services at the Inglewood and Marina del Rey hospitals as a condition of the $55 million purchase, or provide for them in some other way.

"While we don't believe that Catholic hospitals should be able to limit health access, they feel they have a right to do so. Tenet has no right to do so. It's a business decision," said Susan Fogel, legal director of the Women's Law Center.

The loss of reproductive services at hospitals once they merge into Catholic health systems is a major issue among women's health advocates. Less has been said about the maintenance of bans on abortions or other services once hospitals emerge from Catholic systems.


**Choice: Law group seeks a change in policy at Freeman hospitals.**

## Tenet's Catholic system

Buying Catholic hospitals has become a standard strategy for Tenet, which already operates seven hospitals nationwide under the Ethical and Religious Directives for Catholic Health Care Services. It also has another purchase pending in St. Louis.

The chain, the nation's second largest with 114 acute-care hospitals, denies it is reducing reproductive services by not offering them at hospitals that had not been doing so anyway.

Tenet owns Centinela Hospital Medical Center, which is about a mile away from Daniel Freeman Memorial Hospital in Inglewood. Centinela offers a broad range of reproductive services, notes Harry Anderson, Tenet's chief spokesman. "This transaction, if it is approved, will not take away any services to women," he said.

Moreover, Tenet had to agree to abide by the reproductive directive in order to even bid for the hospitals, which are owned by **Carondelet Health System**, a Catholic hospital chain based in St. Louis, he said.

Carondelet issued a statement affirming that such a pledge was a precondition for any bidder.

"These directives have been part of the operating guidelines since the (Inglewood) facility was founded more than 50 years ago," read the statement. Carondelet purchased the Marina hospital in 1980.

Deputy Attorney General Chet Horn said Tenet's agreement to abide by the ethical directives is a top concern of the office, which must review the effects of any sale on the availability of health care in the community. But he conceded that it might be hard to prove the sale would limit care.

"It is difficult to argue when you are talking about a Catholic hospital that has never provided reproductive services, and when this transaction simply continues the status quo," he said.

## Emergency services an issue

Horn said he was equally concerned that Tenet, as part of the agreement, was guaranteeing continued emergency services for only two years. He said the Inglewood facility's emergency room in particular is heavily used.

(In response, Anderson said Tenet plans to continue operating the hospitals as acute care facilities and views emergency services as an "essential element" of such hospitals.)

Despite Tenet's assertions that reproductive services would not be reduced, Fogel said the law center plans to push to have Tenet make some additional services available. That could include offering funding for other providers of such services, or setting up off-site clinics.

The law center also plans to make its concerns heard at a public hearing the state has scheduled on the sale for Oct. 18 at Inglewood City Hall.

Anderson said any new conditions placed on the sale that would raise its costs would not be acceptable to Tenet, which already has agreed to spend $50 million over 10 years to improve the hospitals and expand their services.

# Washington Post

Washington, DC

THURSDAY FEBRUARY 7,2002


# Calif. Hospital Chain Sued; Anti-Latino Bias Alleged

By DAVID S. BRODER
*Washington Post Staff Writer*

LOS ANGELES, Feb. 6—Tenet Health Care Corp., a giant California-based hospital chain, was sued today by a conservative-backed group on charges that it has severely overcharged Latino patients and turned their unpaid bills into higher subsidy payments from the state and federal governments.

The suits, filed in Orange County Superior Court, were announced at a news conference arranged by K.B. Forbes, a former press aide to presidential candidate Patrick J. Buchanan and other conservative notables. Forbes said he has spent much of the past year collecting evidence against Tenet from Latinos he said have had their credit ratings damaged and their lives disrupted as they struggled to pay what he termed inflated Tenet bills.

A Tenet official rejected the allegations and said the company had tried to persuade the plaintiffs' attorney to hold off the lawsuit until the case could be investigated and possibly settled.

Larry Jackson, the Indianapolis attorney for Consejo de Latinos Unidos, the tax-exempt foundation Forbes started to work on the problems uncovered in his investigation, said Tenet was charging these uninsured patients "anywhere from four to seven times" as much as it would HMO patients for similar services.

Harry Anderson, a vice president of Tenet, acknowledged that rates for individual patients are typically higher than those for members of groups that have negotiated with Tenet—a practice he said is typical of the health care industry.

Jackson said, even conceding that, the disparities alleged in the suits are "so extreme" that they violate the California fair business practices statute, which says that hospitals and doctors may collect only "reasonable and customary charges." He said, "Tenet has shown a real tendency to discriminate against and exploit those most vulnerable in this society. This is the kind of thing the courts will try to remedy."

Anderson denied the discrimination charges and called the lawsuits a "misguided ill-advised legal broadside, combined with a media onslaught, intended to inflicted damage on Tenet. We will vigorously defend ourselves." informed The suits also allege that when the "inflated" bills cannot be paid, Tenet writes them off as "charitable care." The more such care it claims, the greater the amount of "DSH funds" it can collect from state and federal governments for its "disproportionate share" of services to indigents. Jackson and Forbes said their analysis of Tenet's financial reports indicated that DSH funds accounted for 38 percent of its net income in California.

Anderson said the premise of this allegation is "flat wrong," because "unpaid bills do not qualify for DSH payments; only charity cases do. We dispute that anything improper or illegal has taken place."

Tenet owns or operates 111 hospitals in 17 states, with the largest number in California. Last month, it reported a quarterly increase of per-share earnings of 43 percent over the same quarter last year and said it expected earnings for the full fiscal year to be up 35 percent from 2001.

The suits alleges that Maria Reyes was billed $15,865 after spending three hours in the emergency room and three days in a Tenet hospital. "An HMO patient would have been charged one-third to one-tenth of the amount," it said.

Forbes distributed a summary of about two dozen cases of similar alleged overcharges he had collected in a year of interviewing Latino families in Southern California. A Spanish-speaking publicist, whose mother is Chilean, Forbes said he "stumbled on the problem" while testing the market for a new form of medical insurance and decided to launch an investigation with the help of Spanish-language media in California.

The New York Times

WEDNESDAY, NOVEMBER 6, 2002

# F.T.C. Opens Inquiry Into Hospital Merger

By REED ABELSON

As part of a broad inquiry into the impact of hospital mergers, federal regulators are seeking information about the 1999 merger of two Missouri hospitals owned by **Tenet Healthcare**, the company said yesterday.

Investors, already concerned about a federal raid at a Tenet hospital in California last week, reacted nervously to the disclosure.

Tenet's stock fell as low as $23.70 yesterday before closing at $26.22, down 78 cents.

"It's a sell now and think about it later kind of market," said Sheryl Skolnick, an analyst at Fulcrum Global Partners, a New York research firm. Ms. Skolnick, who is neutral on the stock, said that she believed investors had overreacted to the news.

The Federal Trade Commission failed in an attempt to block the merger of two Tenet-owned hospitals in Poplar Bluff, Mo., one of several instances in which courts have rebuffed the agency. The F.T.C. said in August that it planned to review various mergers to see how they have affected healthcare, so most analysts said they had expected the inquiry into the Tenet deal.

"We are analyzing several consummated hospital mergers to assess both potential anti-competitive effects and synergies and efficiencies that hospital systems have realized," Michael Cowie, an assistant director of the F.T.C., said yesterday.

Employers and others have voiced concerns that some hospitals have abused their power in some markets to raise prices inappropriately.

Tenet said it believes any review of its performance in Poplar Bluff will show that the merger benefited the community.

Tenet also issued a statement yesterday concerning its Palm Beach Gardens Medical Center in Florida, where the company has been under regulatory scrutiny because of problems with infection control. The company said that the hospital was taking corrective action, and that government officials are now at the hospital to determine that the problems are being resolved.

Analysts have criticized Tenet's handling of last week's news about a raid at its Redding Medical Center in California, where federal authorities are seeking information about possible unnecessary surgeries by two heart doctors. The company has hired Mercer Consulting Group to help it review the doctors' performance.

Tenet also plans to review two to three dozen other high-volume programs at its hospitals in specialties like cardiology and orthopedics, according to Harry Anderson, a company spokesman.

"We are doing it as a precaution," said Mr. Anderson, to ensure that the hospitals and doctors are complying with all of the company's policies and procedures.

Investors are also demanding more information about Tenet's dealings with Medicare, reflecting concern that too many patient cases are considered exceptions under reimbursement rules. Exceptions require higher reimbursements, and investors worry that too many such cases can result in a higher level of regulatory scrutiny. The company has promised to hold a conference call with analysts later this week to provide more information about Medicare reimbursement for exceptional billings.

San Francisco Chronicle
NORTHERN CALIFORNIA'S LARGEST NEWSPAPER
FRIDAY, NOVEMBER 8, 2002

# Management shakeup follows Tenet probe

## Hospital chain's stock falls amid billing questions

By Sabin Russell
and Carolyn Said
CHRONICLE STAFF WRITERS

Embattled hospital chain Tenet Healthcare Corp., whose Redding Medical Center is being probed for unnecessary heart surgeries, has shaken up its top management amid a widening investigation of its nationwide billings to Medicare for high-cost procedures.

Wall Street concern over this complex Medicare billing issue, called "outlier" payments, was building just as the news broke last week of an FBI raid on Redding Medical Center and its two top heart specialists, Chae Hyun Moon and Fidel Realyvasquez Jr.

Investors have been pummeling Tenet shares, which are down 44 percent from only two weeks ago – a staggering loss of nearly $11 billion in market value. The fear is that if Medicare authorities disallow some or all of Tenet's lucrative outlier payments, the corporation might be liable for millions in returned income and penalties.

On Thursday, the Santa Barbara company said its chief financial officer had resigned and its chief operating officer had retired. Tenet chairman Jeffrey Barbakow said he had found fault with the company's "aggressive pricing strategies." He said while the pricing was legal, it was "not the way I want to do business."

Outliers are complex procedures that qualify for higher payments from Medicare because the cost of performing them is significantly higher than national norms.

The executive shakeup comes one day after the Department of Health and Human Services announced it was investigating whether Tenet was overbilling Medicare at its 113 hospitals for outlier procedures.

Meanwhile, an analysis of Medicare records by the powerful California Nurses Association – which is locked in a labor dispute with Tenet at two East Bay hospitals – for the first time links the corporation's "outlier" problem to its Redding hospital.

The union analysis found that 43.3 percent of the Medicare billings from Redding Medical Center were outliers.

That compares to a national average of only 3.5 percent of Medicare payments qualifying for outlier status. Tenet's 113 hospitals across the country had outlier rates averaging 10 percent of total Medicare billings – triple the national average.

Only one hospital in California had a higher rate of outlier payments – Doctors Medical Center in Modesto, a Tenet-owned hospital where outliers made up 49 percent of Medicare payments.

Outlier payments kick in if a hospital can convince an insurer that processes Medicare claims that its costs are higher than allowed in a complex formula.

"If those costs used in the formula are inflated, then Tenet would be in serious trouble," said Don DeMoro, executive director of the Institute for Health and Socio-Economic Policy, which conducted the union analysis. "That's why they are being investigated."

In California, outlier payments accounted for 14 percent of payments to Tenet hospitals, compared to a statewide average of 5.4 percent. If the 40 Tenet hospitals in California were removed from the mix, the statewide average falls to 4.5 percent, according to DeMoro.

Tenet spokesman Gary Hopkins said Thursday he couldn't comment on the specifics of the union analysis. "Obviously the California Nurses Association is attempting to organize Tenet's hospitals in the state. Their press release ought to be taken in that light," he said.

Hopkins also stressed that the investigation of the Redding doctors and the concerns over Medicare billings are "two unrelated issues." It is the doctors, rather than the hospital, who are the targets of the Redding probe, he said.

Within the investment community, the outlier issue overshadows the potential scandal in Redding.

On Thursday, Tenet took steps to try to clean up its image, holding a lengthy conference call with increasingly hostile Wall Street analysts to explain the housecleaning in its executive suites and defend its reliance on outlier payments.

Barbakow said Tenet hospitals' emphasis on teaching programs and surgical specialties explain its many outlier payments. Outlier payments to Tenet went from $351 million in 2000 to $564 million in 2001 and $763 million in 2002.

Barbakow admitted that aggressive pricing contributed to the surge.

"As I carefully studied our Medicare outlier situation over the last two weeks, it became clear to me that formulas that drive these outlier payments were affected by our overall pricing," Barbakow said in a prepared statement. "In some cases, particularly aggressive pricing strategies created increasing outlier payments. That's simply not the way I want to do business at Tenet, nor do I want such a perception to exist in anyone's mind."

Tenet's chief operating officer, Thomas B. Mackey, 54, retired, and its chief corporate officer/chief financial officer, David L. Dennis, 53, resigned. The company's treasurer and senior vice president, Stephen Farber, 33, will become CFO.

Tenet has created a new position of president, reporting to Barbakow. Trevor Fetter, 42, currently CEO of Broadlane, a Tenet spin-off that helps hospitals manage costs, will fill that role.

On Thursday, Tenet closed at $27.95, up $1.67, but fell as low as $17.74 in after-hours trading.

*E-mail the writers at srussell@sfchronicle.com and csaid@sfchronicle.com.*

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# Profiting from health care

LANCE IVERSEN / The Chronicle
Karen Zapata of San Franciso holds her baby daughter, born at a Tenet hospital that Zapata says is burying the family in bills.

## Hospital chain's steep prices blamed for raising costs for all

By Carolyn Said
CHRONICLE STAFF WRITER

Federal investigations of Tenet Healthcare Corp., one by the FBI and the other by Medicare, raise troubling questions about the aggressive tactics used by the nation's second-largest for-profit hospital chain in its pursuit of profits, health care experts say.

Tenet's strategy, as the company explained to admiring Wall Street analysts when its stock was on the rise, is three-pronged: raise prices, cut costs and try to dominate regional markets.

The strategy has hurt consumers nationwide and especially in California, according to health care professionals and consumer advocates. They say it has inflated costs for hospital care, run up taxpayer-funded Medicare bills and increased the amount some insurers pay — which ultimately gets passed on to their customers.

In California, where Tenet

► TENET: Page A10 Col. 1

## Tenet hospital charges in California

*For five procedures that account for the greatest proportion of in-patient charges in California in 2000, prices at Tenet's 41 hospitals were significantly higher than at the state's other 410 hospitals.*

| Procedure | Tenet charges | Other hospitals average | Difference |
|---|---|---|---|
| Tracheostomy | $569,672 | $336,579 | 69% |
| Vaginal birth | 9,582 | 8,628 | 11 |
| Pacemaker implant | 73,038 | 40,452 | 81 |
| Respiratory system diagnosis | 156,769 | 87,809 | 79 |
| Major joint & limb reattachment | 73,791 | 38,093 | 94 |

*Source: Office of Statewide Health Planning and Development (OSHPD), Patient Discharge Data, as analyzed by Service Employees International Union*

# Tenet blamed for raising health costs for all

▶ **TENET**

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owns 42 of the state's 450 hospitals, the hospital chain charges far more than rivals for identical medical procedures.

In 2000, for example, Tenet's California hospitals charged an average of $73,038 for pacemaker implants, 81 percent more than the $40,452 charged by non-Tenet hospitals, according to state government figures analyzed by the Service Employees International Union. Tracheostomies, at $569,672, were 69 percent higher at Tenet than in the rest of the state, where they average $336,579.

"Tenet is engaged in turbo-charging," said Steve Askin, health care research coordinator for the union in Los Angeles. SEIU has a contentious relationship with Tenet over union and insurance issues.

"The company is using its market power to negotiate agreements which are tremendously pushing the pace of health care inflation," Askin said. "That ripples through the entire health care system. The cost is passed on to all of us as consumers."

Now the spotlight has turned on Tenet. Two doctors at its Redding Medical Center are under investigation for allegedly performing unnecessary heart surgeries, and Medicare is probing Tenet's high rate of unusually expensive cases.

■ **Tenet in California:** Tenet's prices are particularly steep in the state, which is its biggest market.

"Tenet's gross charges in California average between six and seven times its actual cost of delivering care," said Askin. For every dollar Tenet hospitals billed, he said, their actual cost was about 16 cents, according to state records. California's non-Tenet hospitals had an actual cost of about 36 cents for every dollar billed.

Tenet's price increases in California also outpace the competition. Tracheostomy charges increased 38 percent from 1999 to 2000 at Tenet hospitals, versus 13 percent at other California hospitals. Respiratory treatment with ventilator support increased 47 percent at Tenet facilities, compared with 22 percent at non-Tenet hospitals.

"Tenet is driving up the cost of health care in California for everyone," said Don DeMoro, executive director of the Institute for Health and Socio-Economic Policy, a nonprofit research group in Oakland. "Many of the charges for various cases and DRGs (diagnostic-related groups) are double for what everyone else is charging. That's an enormous red flag."

■ **How pricing works:** Like most hospitals, Tenet doesn't actually collect the full amount it charges. Similar to a manufacturers' suggested retail price, a hospital's "uniform customary charges," also called "chargebacks," are open to negotiation. Insurers, Medicare, Medicaid, Medi-Cal and HMOs negotiate or set lower rates.

But the "sticker prices" are used to calculate how much Tenet collects in supplemental fees from state and federal agencies such as Medicare; high list prices trigger higher payments. They also can figure into what some insurers pay. And the full sticker prices are billed to those who can least afford to pay them — people who don't have insurance.

Kenny Kwang, who manages the accounting and reporting section for the state's Office of Statewide Health Planning and Development, took a closer look at the charges at Tenet's Redding Medical Center compared to Mercy Medical Center, a hospital in Redding of similar size.

Redding Medical Center's average charge per in-patient day in 2001 was $15,636. Mercy's average was $6,407 — almost 60 percent lower.

Neither hospital actually collects those full charges, but, thanks to its higher markup, Tenet's Redding Medical Center makes out far better than its rival.

Redding Medical Center collected an average of $3,182 per in-patient day, while Mercy received $2,088. So the center's take for every day a patient spends in its hospital is 50 percent higher than that across town at Mercy.

■ **Insurance costs:** Even though insurance rates are negotiated, Tenet's steep sticker prices help increase how much it collects.

The company said as much in a conference call with analysts Nov. 7.

"Higher charges have been a part of our managed-care pricing strategy, particularly in California," said Tenet CEO Jeffrey Barbakow.

Tenet has relied on "stop-loss provisions" to increase payments from insurers. Stop-loss provisions require insurers to reimburse Tenet more than the set per-diem for expensive cases. High list prices would trigger the stop-loss clause more often.

Stop loss "has become a back-door way (for hospitals) to rapidly increase compensation," said Chris Ohman, vice president at Blue Shield of California.

A hospital often can charge its list prices to insurers when people seek medical care outside their regular network – if they fall ill while traveling, for example.

Karen Zapata of San Francisco was six months pregnant and on the highway headed to Los Angeles when she went into premature labor last year. Her husband, John Avalos, rushed to the nearest hospital, Tenet's Sierra Vista Regional Medical Center in San Luis Obispo, where their daughter was born on Christmas Day and received "exemplary" medical care for the next two months, they said.

But the bills were another story. They've received an avalanche of bills for tens of thousands of dollars, the difference between what their insurer paid and what Tenet charged. "It's been very stressful," Avalos said. "There's just no beginning or end to the bills we receive. Right when we think we've got everything settled and seen our last notice, we get another one in the mail."

■ **Outlier payments:** Analogous to the stop-loss provision with private insurers, Medicare has a special allowance to pay extra for expensive cases called outliers. Tenet collects more than three times as much in outlier payments as its nearest rivals, according to an analyst at UBS Warburg, whose report on the issue two weeks ago started a slide in Tenet's stock.

While outliers account for 3.5 percent of Medicare reimbursements at most hospitals, at Tenet they account for 10 percent. In California, 14 percent of Tenet's Medicare payments are outliers, compared with a 5.4 percent average statewide.

More than half of Tenet's outlier payments are concentrated in 11 of its 113 hospitals. Seven of the most outlier-reliant hospitals are in California. They are: Redding Medical Center, Doctors Medical Center of Modesto; USC University Hospital in Los Angeles; Encino-Tarzana Regional Medical Center in the San Fernando Valley; Garfield Medical Center in Monterey Park (Los Angeles County); Centinela Hospital Medical Center in Los Angeles and Desert Regional Medical Center in Palm Springs.

The U.S. Department of Health and Human Services launched a probe of Tenet's excessive outlier reimbursements last week, and the agency that oversees Medicare and Medicaid has said it will close the loophole that allowed Tenet's high prices to trigger so many outlier payments.

■ **HMO withdrawals:** In the past couple of years, Shasta County, where Redding Medical Center is located, has lost all its HMO plans. HMOs said they pulled out because it was too expensive to do business there, citing the limited competition in a two-hospital town, the small pool of doctors – and the high sticker prices at Redding Medical Center. While HMOs increasingly are leaving other rural counties for similar reasons, Shasta still appears to stand out, both in cost and in treatment rate.

"In Shasta, we were seeing admits (hospital admissions) that were around two times higher than what we'd see in our book of business for the rest of the state," said George Anderson, a vice president at Health Net in Woodland Hills (Los Angeles County). Health Net pulled out of Shasta County in 1999. "Some of the more elective procedures, particularly in the surgical area, such as hysterectomies and colon surgeries, were much higher – three or four times more than the rest of the state."

An analysis of state data by the service employees union shows that Tenet's charges in Shasta outpace its rivals by big margins. For a coronary bypass with cardiac catheterization, Tenet's Redding Medical Center charged $228,793 in 2000 – 184 percent more than the average $80,500 charged by the other four hospitals in Shasta County.

"Managed care is not at work there," said Daniel Zingale, director of the California Department of Managed Care, which oversees HMOs. "In places where care is unmanaged, it's not surprising to see overutilization, inappropriate treatment, unnecessary costs."

■ **Uninsured patients:** Like most hospitals, Tenet charges uninsured people the full list price for medical procedures.

Uninsured people lack the resources to pay huge medical bills. But by charging them high prices, Tenet can run up a large figure for bad debt. That is then used to calculate how much state money Tenet collects for charity cases, said K.B. Forbes, spokesman for Consejo de Latinos Unidos. The Los Angeles advocacy group for Latinos has filed several lawsuits accusing Tenet of predatory pricing for uninsured patients.

"We think it is part of a corporate culture that looks at opportunity and tries to aggressively collect money and make profits," Forbes said.

In the past week, Tenet's Barbakow has conceded that the company was aggressive in setting and raising charges and promised to review and rein them in.

Tenet's approach to pricing is not necessarily illegal. Nevertheless, a range of observers, including ordinarily profit-focused Wall Street analysts, have begun to question the ethics behind charging so much for health care.

"I think their pricing policies were designed in bad faith," said Darren Lehrich, vice president of health care analysis for SunTrust Robinson Humphrey, a New York investment firm. "I don't know any other way to put it. They have a duty not to manipulate their strategies to game the system. They just did not act as good corporate citizens."

*E-mail Carolyn Said at* csaid@sfchronicle.com.

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# Bay Area pays dearly for Tenet

## Other hospitals charge about half as much, data show

By Carolyn Said
CHRONICLE STAFF WRITER

Embattled Tenet Healthcare Corp., battered by a stock plunge and two federal investigations, charges Bay Area customers almost twice as much on average for medical procedures as competing hospitals, according to state data.

Tenet's three Contra Costa hospitals charged an average of $51,040 for all in-patient stays in 2000, according to patient discharge data from the California Office of Statewide Health Planning and Development, as analyzed by the Service Employees International Union. That was 98 percent more than the average $25,827 the county's other six hospitals charged.

Tenet's Community Hospital of Los Gatos averaged $40,109 for in-patient stays, 99 percent more than the $20,148 average at Santa Clara County's other 10 hospitals.

"Yes, our rates do tend to be higher," said Tenet spokesman Greg Harrison. "We're reviewing our pricing strategy. We have announced that."

However, he said, across the board, the case mix — a factor that indicates the complexity of the cases — is higher for Tenet than

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for non-Tenet hospitals.

"We're treating more-complex cases or sicker patients and more of them," Harrison said. "That accounts for some of the disparity."

Tenet's high charges became a focus last week for Medicare investigators concerned by the company's high incidence of unusually expensive cases. At the same time, two doctors at its Redding Medical Center have been targeted by an FBI probe of whether they ordered unnecessary heart surgeries.

In Contra Costa County, Tenet's case mix is 1.26, indicating that its cases were 26 percent more complex than the average. In Santa Clara County, Tenet's cases were 13 percent more complex, according to a standardized government measure.

"It sounds like (Tenet's) prices may have been higher than you would expect, even given the power they have in some of the markets they're in," said Joanne Spetz, an economist and professor at UCSF's department of community health systems.

In for-profit health care, such tactics are not unusual, she noted. "Lots of hospitals are pushing the margin on their billing," she said. "They're trying to get as much money as they legally can."

### Higher than rivals

For specific procedures that account for the lion's share of in-patient charges, Tenet's Bay Area charges ranged from 27 to 98 percent higher than those at nearby rivals in 2000.

For example, the 594 women who had vaginal deliveries at Tenet's Community Hospital of Los Gatos were charged an average of $11,137 for their hospital stay. That was 77 percent more than the average $6,297 the other 10 Santa Clara County hospitals charged.

At Tenet's three Contra Costa County hospitals — Doctors Medical Centers of San Pablo and Pinole, and San Ramon Regional Medical Center — patients receiving a pacemaker implant or coronary artery stent implant were charged an average of $95,780 for their hospital stay, almost double the average charge of $48,350 at the county's other six hospitals.

Hospitals don't collect the full amount they charge. However, charges are used to calculate how many unusually expensive cases, called outliers, are entitled to extra Medicare reimbursements. Charges also can figure into how much insurance companies pay when cases cost more than a set per-diem.

### Stock value down 70%

Once a Wall Street darling, Tenet has lost about 70 percent of its stock value — $15 billion in market capitalization — in the past two weeks as investors fretted about the two investigations.

Tenet Chairman and CEO Jeffrey Barbakow told Wall Street analysts he only recently became aware of the aggressive pricing strategy that was spearheaded by Thomas Mackey, the chief operating officer, and David Dennis, the chief financial officer. Both executives stepped down last week.

Barbakow said the company has done nothing illegal but promised to audit its charges and be less aggressive in its pricing.

In Shasta County, where Redding Medical Center was raided by 40 FBI agents two weeks ago, Tenet's charges stand out even more.

The type of heart procedures under investigation are dramatically more expensive, as well as more common, at RMC than at the county's four other hospitals.

RMC did 532 coronary bypasses, charging an average of $228,793. The other hospitals did 206 of the procedures, charging $80,500.

At RMC, there were 604 pacemaker or stent implants averaging $89,787, versus an average $45,500 for the 264 similar such procedures at rivals.

And for cardiac valve and other major cardiothoracic procedures with cardiac catheterization, RMC charged $330,959 on average and performed 161 procedures. The nearby facilities charged $143,188, but performed only 40 procedures.

With 42 of California's 450 hospitals, Tenet is the largest hospital operator in the state. It is the second-largest for-profit hospital chain in the country.

*E-mail Carolyn Said at* csaid@sfchronicle.com.

## Tenet hospital charges, 2000

*For procedures that account for the greatest proportion of in-patient charges in specific counties, average charges at Tenet hospitals were compared to those at non-Tenet hospitals. Charges are for the entire length of a patient's stay related to a specific diagnostic-related group.*

### CONTRA COSTA COUNTY

| Diagnostic-related group | Tenet charge | Other hospitals charge | Difference |
|---|---|---|---|
| Pacemaker implant | $95,780 | $48,350 | 98% |
| Tracheostomy, complex* | $608,296 | $401,496 | 52% |
| Coronary bypass w/cardiac cath. | $192,136 | $150,719 | 27% |
| Heart failure and shock | $41,645 | $23,844 | 75% |
| All diagnostic-related groups** | $51,040 | $25,827 | 98% |

**Tenet hospitals:** Doctors Medical Center of San Pablo, Doctors Medical Center of Pinole, San Ramon Regional Medical Center

**Non-Tenet hospitals:** Contra Costa Regional Medical Center, Sutter Delta Medical Center, John Muir Medical Center, Mt. Diablo Medical Center, Walnut Creek Hospital, San Ramon Rehabilitation Hospital

### SANTA CLARA COUNTY

| Diagnostic-related group | Tenet charge | Other hospitals charge | Difference |
|---|---|---|---|
| Tracheostomy, complex* | $598,164 | $408,389 | 46% |
| Vaginal delivery | $11,137 | $6,297 | 77% |
| Pacemaker implant | $69,367 | $35,522 | 95% |
| Neonate, extreme immaturity or respiratory distress | $101,175 | $197,407 | -49% |
| Major joint & limb reattachment | $62,796 | $38,482 | 63% |
| All diagnostic-related groups** | $40,109 | $20,148 | 99% |

**Tenet hospital:** Community Hospital of Los Gatos

**Non-Tenet hospitals:** Regional Medical Center of San Jose, El Camino Hospital, Good Samaritan Hospital, O'Connor Hospital, San Jose Medical Center, Santa Clara Valley Medical Center, Stanford University Hospital, Lucile S. Packard Childrens Hospital, Childrens Recovery Center of Northern California, St. Louise Regional Hospital

### SHASTA COUNTY

| Diagnostic-related group | Tenet charge | Other hospitals charge | Difference |
|---|---|---|---|
| Coronary bypass w/cardiac cath. | $228,793 | $80,500 | 184% |
| Pacemaker implant | $89,787 | $45,500 | 97% |
| Cardiac valve w/cardiac cath. | $330,959 | $143,188 | 131% |
| Tracheostomy, complex* | $1,105,076 | $447,821 | 147% |
| Major joint & limb reattachment | $74,983 | $36,066 | 108% |
| All diagnostic-related groups** | $78,975 | $23,070 | 242% |

**Tenet hospital:** Redding Medical Center

**Non-Tenet hospitals:** Mayers Memorial Hospital, Mercy Medical Center, Northern California Rehabilitation Hospital, Patient's Hospital of Redding

*For cases in which a critically ill patient requires prolonged mechanical ventilation in the intensive-care unit.

**Encompasses all in-patient cases in all diagnostic categories.

*Source: Office of Statewide Health Planning and Development (OSHPD), Patient Discharge Data, as analyzed by the Service Employees International Union.*

*Chronicle Graphic*

San Francisco Chronicle
NORTHERN CALIFORNIA'S LARGEST NEWSPAPER
Tuesday, November 19, 2002

# SEC probing Tenet

By Carolyn Said
CHRONICLE STAFF WRITER

Tenet Healthcare Corp. on Monday said that the Securities and Exchange Commission is informally investigating it in the wake of a stream of revelations that have battered the company's stock during the past three weeks.

Tenet met with representatives of the SEC's Pacific regional office last week to discuss its receipt of unusually high numbers of a type of expensive Medicare reimbursement called outliers, as well as the huge trading volume in the company's stock, Tenet Chief Executive Officer Jeffrey Barbakow wrote in a letter to shareholders.

Santa Barbara's Tenet, the nation's No. 2 for-profit hospital chain, has lost about 70 percent of its value – about $17 billion in market capitalization – since late October.

The stock slide began when a Wall Street analyst questioned the company's reliance on outlier payments, then accelerated when FBI agents raided its Redding Medical Center for a probe of whether two doctors there had ordered unnecessary heart surgeries for patients.

Medicare launched its own probe of the outlier payments two weeks ago, which further battered the stock. After reaching a 52-

▸ TENET: Page B2 Col. 3

# Informal SEC investigation of Tenet trading, outliers

▸ **TENET**
*From Page B1*

week high of $52.50 on Oct. 3, it plunged to as low as $14 by Nov. 11.

"The speed and extent of the devastation to Tenet's stock and its reputation in less than three weeks has been shocking," Barbakow wrote.

Wall Street analysts were sanguine about news of the SEC informal probe.

"This is normal course for a company that's seen its share price so devastated in such a short period of time," said Darren Lehrich, vice president of health care equity research at investment firm SunTrust Robinson Humphrey.

Tenet's Barbakow also said the company has repurchased 10 million shares, reaching the maximum allowed for this time period. That seemed to reassure jittery investors, who took it as a sign that there is no more bad news lurking. Tenet's stock rebounded 14.8 percent, or $2.42, to close at $18.75 Monday.

Tenet said that the Joint Commission on Accreditation of Healthcare Organizations had initiated a quality review of its hospitals. The company said it already has launched its own similar review after the Redding raid.

Tenet is also reviewing its aggressive pricing strategies because of concerns that it receives more outlier payments than any other hospital chain. Barbakow's letter laid the blame for the aggressive pricing even more squarely on two departed executives, Chief Operating Officer Thomas Mackey and Chief Financial Officer David Dennis, saying he previously had been trying to protect their reputations. Mackey and Dennis both left the company on Nov. 7.

"Once I became fully aware of the aggressiveness of pricing strategies in certain markets and of the corollary impact on outlier payments, I realized that the company's credibility would be shattered," Barbakow wrote.

In regular SEC filings last month, the company disclosed that Mackey sold 278,000 shares of Tenet stock on Oct. 4 at $51.50 per share for a total of $14.3 million – a few weeks before the dramatic stock slide began.

Barbakow's letter said that the departures of the CFO and COO were directly linked to the aggressive pricing strategy and weren't symptoms of any deeper problems.

*E-mail Carolyn Said at csaid@sfchronicle.com.*

San Francisco Chronicle
NORTHERN CALIFORNIA'S LARGEST NEWSPAPER
WEDNESDAY, NOVEMBER 20, 2002

# Tenet raises prices more quickly than competitors

## Union asks state to look at charges

*By Carolyn Said*
CHRONICLE STAFF WRITER

Tenet Healthcare Corp. has raised its California hospital charges dramatically, outpacing its rivals by wide margins, as part of the company's aggressive pricing policy now under federal scrutiny.

Tenet's charges rose by 31 percent between 1999 and 2000, while those at other state hospitals increased by 24 percent, state data show.

In the 10 California counties where Tenet operates, its average charge for a hospital stay was $33,547, 63 percent more than at other state facilities, according to patient discharge data from the California Office of Statewide Health Planning and Development as analyzed by the Service Employees International Union.

The SEIU, which quarrels with Tenet over union and insurance issues, called on the California Public Employees' Retirement System (CalPERS) Tuesday to look into Tenet's pricing and medical practices.

The numbers are adjusted to

▶ **TENET:** *Page A15 Col. 1*

▶ **TENET**
*From Page 1*

account for case mix, a government measure of the complexity of cases; Tenet has said that its high charges are in part due to treating more complex cases. The 2-year-old data are for the most recent period available.

Hospital charges, similar to the sticker price for cars, ordinarily are not paid in full. But they help determine payments for unusually expensive cases.

Tenet, the nation's No. 2 for-profit hospital chain and the largest in California, has come under intense scrutiny in the past three weeks. Medicare is investigating whether Tenet's pricing allowed it to collect too many Medicare reimbursements for expensive cases called outliers, and the FBI is looking into whether two doctors at its Redding Medical Center ordered unnecessary heart surgeries and other procedures.

Tenet has acknowledged that its charges were aggressive and said it will review and rein them in. Two top executives, the chief financial officer and the chief operating officer, who the company said spearheaded the high sticker prices, left the Santa Barbara firm two weeks ago.

"The fascinating thing is that raising charges that supposedly nobody looks at results in above-average payment streams from (Medicare)," said John Ransom, managing director of health care research at Raymond James & Associates, an investment firm in St. Petersburg, Fla.

Tenet's outlier payments from Medicare rose from $351 million in 2000 to $564 million in 2001 and $763 million in 2002. Barbakow has said that aggressive pricing contributed to the surge.

"Tenet's done nothing illegal," said spokesman Steven Campanini. "We'll stand by that. ... However, when we took a closer look at this issue (of outlier payments), we found our aggressive pricing strategy, particularly in certain markets, resulted in far higher than average Medicare payments at some of our hospitals."

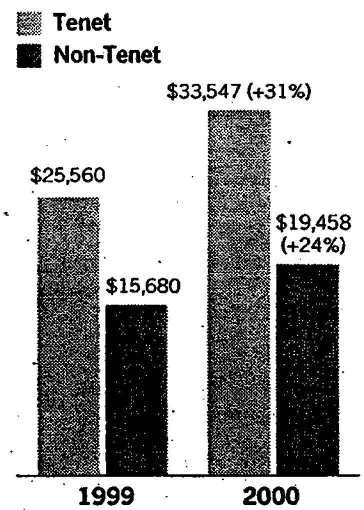
Campanini said some high average charges could result from patients who had prolonged stays. For example, two patients in Contra Costa County spent several years in Tenet hospitals, he said. A full year's charges for each of those patients would have been averaged with the thousands of other treated patients for both 1999 and 2000. (Similarly, long-term patients elsewhere also figured into the averages for non-Tenet hospitals.)

"I was surprised to see how aggressive their pricing is," said Walter Kopp, president of Medical Management Services, a San Anselmo health care consultant to hospital systems. "The case mix (complexity of cases) does not account for the entire difference in their rates."

In some specific counties, the difference between how Tenet and non-Tenet hospitals raised charges is striking.

### Tenet charges in California

*Average charges for all inpatient stays at Tenet and non-Tenet hospitals were compared for 1999 and 2000. Charges are adjusted to account for more complex cases.*




*Source: Office of Statewide Health Planning and Development (OSHPD), Patient Discharge Data, as analyzed by the Service Employees International Union*

*Chronicle Graphic*

# Tenet raises prices quickly

Between 1999 and 2000, Tenet's average charges in Contra Costa County, where it operates three hospitals, rose by 123 percent, while the other six hospitals in the county raised their average charges by 13 percent.

In Riverside and Los Angeles counties, where Tenet operates about one out of every five hospitals, it raised charges two or three times as much as rivals. In Riverside County, Tenet charges rose 27.6 from 1999 to 2000, versus 13.3 percent at other facilities. In Los Angeles County, Tenet's charges rose 29.9 percent, compared with 10 percent elsewhere.

"Tenet tries to get controlling oligopolies in targeted urban and suburban areas," said Albert Lowey-Ball, professor of health policy and economics at Holy Names College in Oakland. "The greater the proportion of the hospital market they have in any area, the greater the freedom they can have in establishing charge structures that would favor them."

Stephen Shortell, dean of the School of Public Health at UC Berkeley, said Tenet had established a "reasonably good reputation" for being well run over the past few years under CEO Jeffrey Barbakow.

That was a far cry from the situation before Barbakow took the helm in 1993. Formerly called National Medical Enterprises, the company faced federal charges of overbilling and patient complaints of imprisonment in its psychiatric hospitals. Barbakow paid over half a billion dollars in civil and criminal penalties to settle those charges, sold off the psychiatric units and changed the company's name and direction, stressing a strict ethical policy.

Shortell said he believed that Tenet had done nothing illegal and was following blueprints similar to other for-profit hospital chains.

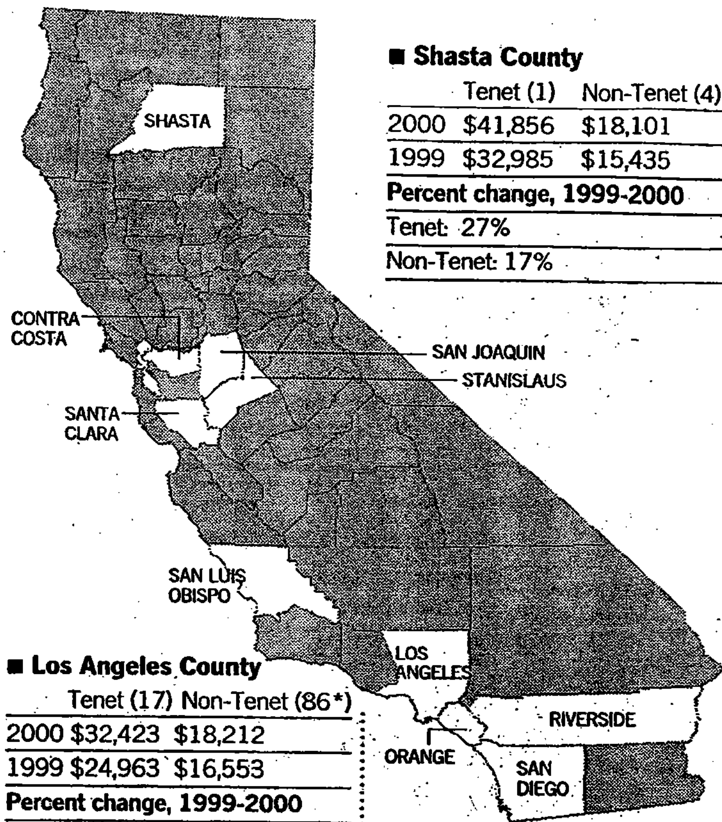
"Historically the nature of investor-owned, for-profit hospital systems is they tend to locate in parts of the country with good socio-demographics. Then, they tend to push to the limit in terms of what insurers and Medicare will pay," he said.

Medicare has said it will fix the loopholes that allowed Tenet to receive so many outlier payments.

Some observers said Tenet may have to return some of the millions of dollars it collected.

## Tenet hospital charges

*Charges at Tenet Healthcare Corp. hospitals in the 10 California counties where it operates were compared to those at non-Tenet hospitals for 1999 and 2000. Charges are averaged from all in-patient stays at the hospitals and are case-mix adjusted to make allowances for more-complex cases. Numbers in parentheses are number of hospitals.*



Source: ESRI, GDT, USGS

### Shasta County

| | Tenet (1) | Non-Tenet (4) |
|---|---|---|
| 2000 | $41,856 | $18,101 |
| 1999 | $32,985 | $15,435 |

**Percent change, 1999-2000**
Tenet: 27%
Non-Tenet: 17%

### Contra Costa County

| | Tenet (3) | Non-Tenet (6) |
|---|---|---|
| 2000 | $40,358 | $23,118 |
| 1999 | $18,073 | $20,519 |

**Percent change, 1999-2000**
Tenet: 123%
Non-Tenet: 13%

### Santa Clara County

| | Tenet (1) | Non-Tenet (10) |
|---|---|---|
| 2000 | $35,346 | $20,625 |
| 1999 | $32,759 | $18,989 |

**Percent change, 1999-2000**
Tenet: 8%
Non-Tenet: 9%

### Los Angeles County

| | Tenet (17) | Non-Tenet (86*) |
|---|---|---|
| 2000 | $32,423 | $18,212 |
| 1999 | $24,963 | $16,553 |

**Percent change, 1999-2000**
Tenet: 29.9%
Non-Tenet: 10%

### Stanislaus County

| | Tenet (1) | Non-Tenet (4) |
|---|---|---|
| 2000 | $55,528 | $25,143 |
| 1999 | $38,010 | $22,756 |

**Percent change, 1999-2000**
Tenet: 46%
Non-Tenet: 10%

### Riverside County

| | Tenet (3) | Non-Tenet (13) |
|---|---|---|
| 2000 | $27,955 | $12,908 |
| 1999 | $21,911 | $11,393 |

**Percent change, 1999-2000**
Tenet: 27.6%
Non-Tenet: 13.3%

### San Diego County

| | Tenet (1) | Non-Tenet (23) |
|---|---|---|
| 2000 | $28,605 | NA |
| 1999 | $23,429 | $13,691 |

**Percent change, 1999-2000**
Tenet: 22%
Non-Tenet: NA

### San Luis Obispo County

| | Tenet (2) | Non-Tenet (3) |
|---|---|---|
| 2000 | $35,727 | $13,021 |
| 1999 | $26,299 | $12,228 |

**Percent change, 1999-2000**
Tenet: 36%
Non-Tenet: 6%

### Orange County

| | Tenet (10) | Non-Tenet (23) |
|---|---|---|
| 2000 | $23,885 | $17,388 |
| 1999 | $19,199 | $14,198 |

**Percent change, 1999-2000**
Tenet: 24.4%
Non-Tenet: 22.5%

### San Joaquin County

| | Tenet (1) | Non-Tenet (6) |
|---|---|---|
| 2000 | $44,908 | $16,115 |
| 1999 | $32,743 | $15,363 |

**Percent change, 1999-2000**
Tenet: 37%
Non-Tenet: 5%

* 86 in 2000 and 87 in 1999

*Source: Office of Statewide Health Planning and Development (OSHPD), Patient Discharge Data, as analyzed by the Service Employees International Union*

*Chronicle Graphic*

The New York Times

TUESDAY, DECEMBER 3, 2002

# Tenet Alters Fee Schedule On Health Care

By Reuters

Tenet Healthcare Inc., seeking to repair its reputation with health plans amid a federal inquiry into unusually high Medicare payments it has received, struck a deal yesterday with Health Net Inc. that alters the way Tenet charges the plans for hospital costs.

The new contract, which covers 27 Tenet hospitals in California, adopts a fixed-payment setup instead of fees based on retail prices.

Tenet, which is based in Santa Barbara, Calif., scheduled a conference call for today to discuss its outlook and a new pricing strategy as regulators examine so-called Medicare outlier payments to Tenet.

Under Medicare, hospitals are typically paid a fixed amount for specific diseases, but they also qualify for special reimbursement if the cost of a case surpasses a certain amount. Tenet, one of the nation's largest hospital chains, has come under scrutiny for collecting an unusually large amount of these payments.

Federal regulators said last month that they planned a companywide audit to make sure the payments were proper under Medicare rules.

Health plans suffer because those payments are based on retail or gross charges — the sticker prices for hospital services, which the plans say are often inflated.

Neil Sorrentino, executive vice president for operations for Tenet's western division, said the new contract would provide the revenue to cover rising hospital costs.

Investors have sold off Tenet stock over concerns about the sustainability of the outlier payments, which accounted for $763 million in revenue in the fiscal year ended in May — a bigger percentage than that of Tenet's peers.

Shares of Tenet have dropped 63 percent since Oct. 25, the last trading day before UBS Warburg downgraded its rating because of the outlier payment issue. Shares of Tenet fell 69 cents yesterday, to $17.76.

Frank Morgan, an analyst at Jefferies & Company, said he expected this deal to be the first of many in Tenet's negotiations with health care payers. The lack of details make it difficult to gauge the effect of the contract on earnings, but it could slow growth, he said.

Modern Healthcare

January 6, 2003

# Justice seeks Tenet outlier info

The U.S. Justice Department subpoenaed Tenet Healthcare Corp., Santa Barbara, Calif., seeking information about Medicare outlier payments made to 19 of Tenet's hospitals from 1997 to 2002, the company said.

Meanwhile, the American Hospital Association confirmed that it is planning a Jan. 7 meeting to educate state hospital association officials about what to expect from new federal audits regarding these payments (See related story, p. 10).

Pearce called for the CMS to halt outlier payments to Tenet.

The Justice Department subpoena represents the latest investigation to be launched in recent months against Tenet. HHS' inspector general's office is already auditing Tenet's outlier payments, which are meant to partially reimburse hospitals for complex cases whose treatment costs far exceed DRG rates. Also, the Federal Trade Commission is reviewing Tenet's consolidation of the only two hospitals in Poplar Bluff, Mo., and federal agents have raided two Tenet hospitals in California in connection to other investigations.

In its "administrative investigative demand subpoena," the Justice Department requested documents from 19 hospitals owned by Tenet in California, Louisiana, Pennsylvania and Texas. Spokesman Harry Anderson said Tenet would comply with the subpoena. "They are expecting us to produce documents by Feb. 4," he said. "We will make every effort to comply with that. It is very early in the process."

One of Tenet's harshest critics, M. Lee Pearce, M.D., who heads the self-appointed Tenet Shareholders Committee, called for the Centers for Medicare and Medicaid Services to halt outlier payments to Tenet and other nonteaching hospitals that are above 7% of total DRG-generated payments.

As for the meeting at AHA headquarters in Washington, spokesman Richard Wade said he expects a big crowd. "There's a lot of concern out there about what this is going to be like and how it's going to go," Wade said. «

Modern Healthcare

January 13, 2003

# A question of integrity

*Federal prosecutors question Tenet's compliance with integrity agreement in a $323 million False Claims Act lawsuit*

Since the hardball business practices of Richard Scott's Columbia/HCA Healthcare Corp. drew unwanted national attention and government scrutiny in the late 1990s, Tenet Healthcare Corp. has pitched itself as the kinder and cleaner for-profit hospital chain alternative, vowing to maintain an acquired hospital's culture.

Last week's $323 million lawsuit filed by the U.S. Justice Department against Tenet was the latest legal woe to sully that carefully manicured reputation. In recent months, Tenet, Santa Barbara, Calif., has become the main course for hungry federal prosecutors, regulators and investigators.

Perhaps most troubling for Tenet is that federal prosecutors are alleging that it violated the 1994 corporate integrity agreement signed by its predecessor, National Medical Enterprises, Santa Monica, Calif. The CIA was signed in conjunction with NME's $379 million settlement—then the largest healthcare fraud settlement to date—of allegations against the company's psychiatric hospital subsidiary. The lawsuit also marks another sign that healthcare fraud enforcers are stepping up their scrutiny of the industry in response to congressional pressure (Dec. 23-30, 2002, p. 6).

## A heap of trouble

Triggered by the one-two punch of a healthcare stock analyst questioning Tenet's earnings and the FBI raid of its Redding, Calif., hospital, the value of its stock has plummeted 70% since the last week of October. A subsequent string of probes has further blackened the company's name—an audit of Tenet's Medicare outlier payments by the HHS' inspector general, a Federal Trade Commission review of a Poplar Bluff, Mo., hospital merger, a raid by agents from HHS' inspector general's office and the Internal Revenue Service at the company's 193-bed Alvarado Hospital Medical Center, San Diego, and a Securities and Exchange Commission investigation.

Tenet's latest black eye came after months of intense negotiations between Tenet and the Justice Department broke off last week. Prosecutors filed the civil False Claims Act lawsuit in U.S. District Court in Los Angeles, alleging that Tenet illegally submitted more than 19,300 false claims for $115 million in wrongfully upcoded Medicare bills in order to maximize revenue. Under the False Claims Act, Tenet faces damages of nearly triple that amount—up to $323 million—plus up to $10,000 per alleged false claim.

Officials from Tenet, which operates 114 hospitals, said the two sides were far apart on the settlement numbers. "We regret that we have been unable to reach an amicable resolution of these issues," Christi Sulzbach, Tenet's chief corporate officer and general counsel, said in a written statement.

In the 15-page complaint, the Justice Department alleged that the upcoding scheme was part of a deliberate corporate plan to optimize DRG coding. The government also accused Tenet of refusing to return the Medicare overpayments and falsely certifying it was complying with its CIA, all in violation of federal law. A Justice Department spokesman said 104 Tenet hospitals are named in the complaint. Department officials declined to comment on the Tenet settlement talks or to specify any added penalties for allegedly violating its CIA.

AP/WIDE WORLD

**Security guards patrol the entrance to Tenet's Alvarado Hospital after the U.S. attorney's office served federal search warrants on two of the hospital's administrative offices.**

### Seeking the ultimate penalty

U.S. Rep. Pete Stark (D-Calif.) said he will recommend to HHS Secretary Tommy Thompson that he revoke the company's certification for Medicare and Medicaid. "How long have we been fighting with these guys and how many times have they walked too close to the edge and stolen money from the government?" Stark asked.

Last month, Stark wrote HHS Inspector General Janet Rehnquist to complain of lax oversight of the CIA he contends the company violated. "I am troubled that many of the current allegations against Tenet appear to stem from behavior that should have been detected, reported and remedied under that CIA," Stark said in his letter.

Ruggio: Justice will use alleged violation as a negotiation tool.

Stark said Tenet officers should go to prison. "We have a serious problem here," Stark told *Modern Healthcare*. "It's not just on the for-profit side, although those guys have it down to a science, but it's on the not-for-profit side of healthcare as well. The temptation and the pressures to produce profits are just too great. The whole industry is becoming fraught with this. And now it's affecting quality."

He said healthcare executives should be held to a higher standard of ethics and compliance than their counterparts at nonhealthcare companies "because mistakes and a cavalier attitude can cause serious harm or even death. At least nobody died at Enron. We're seeing a culture of apathy in healthcare and that's too bad. The government should come down hard on Tenet."

How did Tenet allegedly revert back to the reputation everyone thought it had discarded after the NME settlement? Didn't the rise of Jeffrey Barbakow as the company's chief executive officer and chairman, as well as NME's 1995 merger with American Medical International, bury that in the past?

Thomas Atchison, a healthcare consultant with Atchison Consulting Group, Oak Park, Ill., said corporate culture can explain the recurrence of the problems. Atchison said it's impossible to change a corporate culture "as long as the environment is pressured with a drive for profits in quarterly earnings reports. This week it's Tenet," he said. "Next week it will be someone else. The pressure to exaggerate revenues and cut services is very powerful.

"I think that the healthcare culture of pursuing a profit is a toxic phenomenon that has poisoned the fundamental mission of healthcare," Atchison added. "That won't change until hospitals refocus on why they are in the business to begin with: to take care of patients."

### Coming home to roost

Former Justice Department attorney Michael Ruggio, who worked on the NME settlement and is now a partner with the Washington office of the law firm Duane, Morris & Heckscher, said the alleged violation of the CIA could increase the amount of the alleged damages when the case is eventually resolved.

"The Justice Department will use this as a negotiating lever," said Ruggio, adding that the government takes a dim view of providers who ignore their compliance agreements. A spokeswoman from the HHS' inspector general's office said 767 providers have signed CIAs to date.

Ruggio said in the wake of corporate scandals

*Continued on p. 16*

## COVER STORY >> *from p. 7*

and the escalating costs of healthcare, the Tenet suit represents the latest salvo in a ratcheted-up federal antifraud enforcement effort. "We're seeing increased pressure on Inspector General Rehnquist and the Justice Department, particularly after the inquiries by Sen. (Charles) Grassley (R-Iowa) and the General Accounting Office. What was considered by some as laxity is now moving in the opposite direction."

Ruggio predicted that Tenet's troubles are far from over. "The outlier payment issue will be very big for them, and there's almost no defense for that," he said. "This may not reach the magnitude of HCA, but it could be close."

Young: Allegations raise troubling legal issues for Tenet.

He said when Columbia/HCA faced legal scrutiny in 1997, it found religion, integrating compliance into its corporate culture. "Tenet never got tagged until recently, so in the meantime, its stock soared, and many of the people who were around from NME and AMI remained in power," he said. "Tenet also used a number of revenue-maximizing consultants. It's extremely difficult to modify an existing culture when thousands of employees are ingrained in one way of doing things.... You don't turn it on a dime. It takes years."

### 'Chilling effect' on negotiations

Howard Young, a former deputy chief of the civil recoveries branch at the HHS' inspector general's office and now with the Washington office of law firm Arent Fox, said the Justice Department's allegation that Tenet violated the False Claims Act when it falsely certified compliance with its CIA raises troubling legal issues.

"This is the first time, to my knowledge, that the Justice Department is alleging this to be a false statement under the act. It could have a chilling effect on what historically have been frank and honest settlement talks between the government and providers, which has always encouraged dialogue and honest reporting," he said. "It raises a whole host of issues surrounding corporate integrity agreements. I find it very alarming."

Young, though, said the inclusion of the alleged CIA violations may constitute a negotiating ploy by the Justice Department. "This could be a game of brinksmanship to gain advantage," he said. "This is a classic case of bootstrapping and piling on by the Justice Department."

Young faulted the department for vilifying Tenet in the complaint for failing to repay an overpayment. "Nobody pays back an overpayment while they're negotiating, you pay it back as part of the settlement," he said. "I think that was a cheap shot. The Justice Department is trying to put icing on the cake and paint Tenet as a bad actor. And in light of Enron it can't resist." While Tenet's legal woes may keep the company's lawyers busy for years, stock analysts like SunTrust Robinson Humphrey Capital Market's Darren Lehrich see an upside to the news of the suit. While he said his firm is cautious on the stock, Lehrich said the market was relieved to finally see the amount of the alleged damages.

"They've needed to go through this chapter and quantify the costs of these various investigations," Lehrich said, pointing out that the DRG upcoding issue is not unique to Tenet. "The question you wonder is, 'How much worse can it get?' You don't know what other shoes will drop." «

# The Week in Healthcare

**CHAINS** >> *Vince Galloro*

## Tenet gets ready to sell

### *14 hospitals will be sold or closed, $100 million cut as company aims to reclaim the trust of investors*

Tenet Healthcare Corp. last week took another page out of the Columbia/HCA Healthcare Corp. comeback playbook.

Santa Barbara, Calif.-based Tenet said it is selling or closing 14 hospitals in eight states, cutting costs by $100 million annually and adopting a more transparent accounting policy, all in an effort to rebuild investors' shattered confidence in the company. *Modern Healthcare* first reported last month that Tenet was considering a major divestiture (Feb. 17, p. 12).

"In early December, we laid out for analysts and investors a series of areas where we were going to focus," Tenet President Trevor Fetter said last week in an interview. The company then said that senior management was studying every aspect of its operations in light of the uproar over its Medicare outlier payments, Fetter said. "In the last two weeks, I think that our announcements fall very squarely in the 'taking action' category," he said.

Tenet's situation mirrors Columbia/HCA circa 1997, though on a less drastic scale: executive resignations, hospital sales or spinoffs, corporate restructuring and the adoption of new accounting policies. The moves the company has made over the last five months also draws upon Tenet's "back to basics" strategy, which included the company's last large selloff of hospitals, in 1999.

Nancy Weaver, a healthcare stock analyst with Stephens, an investment bank based in Little Rock, Ark., said Tenet's moves, including the latest announcement, make a lot of sense. "I think investors are still going to be leery in the short term," she said. "Tenet needs two or three quarters to show investors what they're doing."

Tenet's stock has declined by two-thirds since a devastating series of revelations last fall, starting with a stock analyst's report questioning its high Medicare outlier reimbursements and compounded by a raid by federal agents of Tenet's 188-bed Redding (Calif.) Medical Center in a probe of two physicians practicing there. Since then, Tenet's No. 2 and No. 3 executives have resigned, the HHS' inspector general's office started an audit of Tenet's outlier payments, and the U.S. Justice Department filed a $323 million False Claims Act lawsuit against the company alleging widespread DRG upcoding.

Trevor Fetter says the move shows Tenet is "taking action."

Earlier this month, Tenet announced a major reorganization of its hospitals into two divisions from three (March 17, p. 17). In separate announcements, Tenet said it hired F. Scott Kellman as treasurer and senior vice president of corporate finance and real estate and promoted Stephen Newman, a physician, to the new position of CEO of Tenet's 40 California hospitals.

#### Sell-off strategy

Fetter said Tenet waited to announce the divestitures as a group. "We were very eager to put an announcement out and be very specific for the stability of all the hospitals," he said. "It sort of puts everybody's mind at ease, one way or another."

Tenet isn't trying to sell off troubled hospitals, Fetter said. In the fiscal year ended May 31, 2002, the 14 hospitals had a combined net revenue of $933 million and combined operating earnings of $141 million. Tenet had fiscal 2002 revenue of $13.9 billion. Fetter noted that the group had Medicare outlier revenue of only $15 million.

In compiling the list, Fetter said, the key question was, "Is there a single hospital in a geographic location that we own where we don't really have a strategy for growth or adding to a network?" Tenet said it would exit two states entirely—selling its four Arkansas hospitals and its lone Nevada hospital—and would sell or close selected hospitals in California, Florida, Missouri, Pennsylvania, Tennessee and Texas (See illustration).

The proceeds of the sales and the cost savings, which Tenet said would be in "nonpatient care" expenses, all will go toward repurchasing shares of Tenet to bolster their value, the company said. Investors have been clamoring since Tenet's troubles began for the company to start a major share repurchase program.

Weaver, the Stephens analyst, said she estimated Tenet could clear pretax proceeds of $700 million to $800 million on the sales. She said she expected the Houston- and Philadelphia-area hospitals to be very tough to sell. She predicted there would be several bidders for the Tennessee hospitals and said the others also are strong assets.

Fetter said Tenet still thinks there will be buyers for the Philadelphia-area hospitals, although he acknowledged that one of them, 158-bed Elkins Park (Pa.) Hospital, is likely to be converted into a long-term acute-care hospital.

#### Rivals circling

Speculation about potential buyers mostly centered on other investor-owned chains. Fetter confirmed that he had deal discussions with officials from some of the investor-owned companies attending the Federation of American Hospitals' annual meeting in Washington last week.

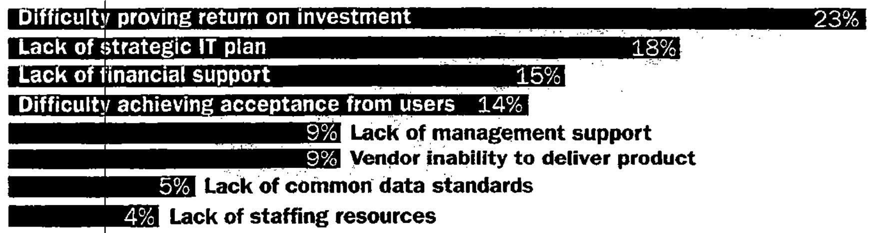
Nashville-based HCA could show interest in the hospitals located in markets where it already has a significant presence, including Florida, Houston, Las Vegas and Tennessee, HCA spokesman Jeffrey Prescott said. "We're going to follow our standard acquisition strategy, and if there's something that fits, we'll take

## BY THE NUMBERS

Proof of benefit is the main obstacle to getting healthcare organizations to implement information technology, according to a survey of consulting and information-systems companies by the Healthcare Information and Management Systems Society. Technology challenges and technical hurdles no longer loom as large, but providers have to be convinced that the costly investment is worth it.

*Source: Healthcare Information and Management Systems Society*

Most significant barriers to IT implementation at client facilities
(Percentage of respondents)




a look at it," he said.

Other sources, who asked that they not be identified, suggested that Triad Hospitals, Plano, Texas, could be interested in the four Arkansas hospitals. Triad already operates five hospitals in Arkansas.

These sources also indicated that Health Management Associates, Naples, Fla., and two Brentwood, Tenn.-based companies, Community Health Systems and LifePoint Hospitals, would likely bid on some of the rural hospitals Tenet is selling.

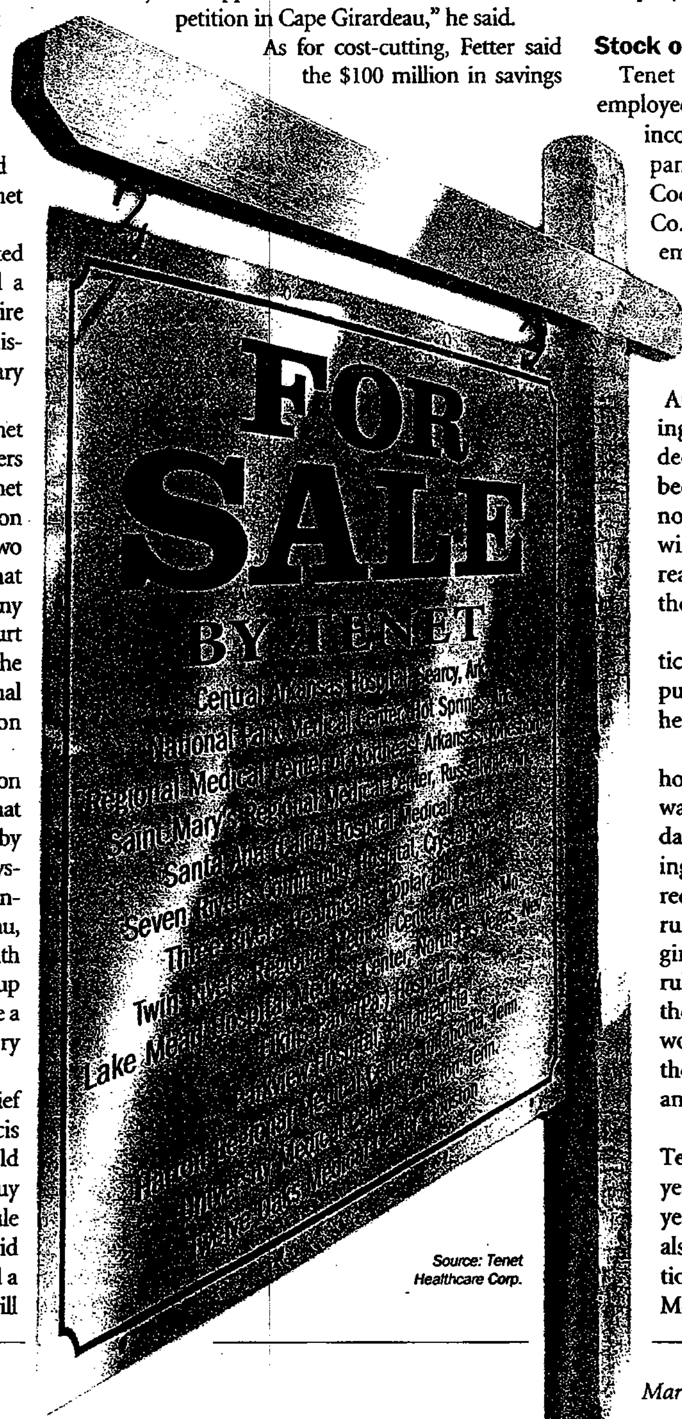
The sources also said they doubted that Tenet would be able to find a buyer who is interested in the entire package, since the hospitals are in disparate areas geographically and vary from large urban to rural markets.

One of the hospitals that Tenet wants to sell is 294-bed Three Rivers Healthcare, Poplar Bluff, Mo. Tenet fought the Federal Trade Commission for two years to consolidate the two formerly competing hospitals that make up Three Rivers. The company eventually won a federal appeals court ruling that allowed Tenet to buy the former 186-bed Doctors Regional Medical Center for $40.5 million (July 26, 1999, p. 2).

The monopoly faces competition from a proposed medical campus that would be a joint venture of a nearby hospital, Saint Francis Healthcare System, which owns 249-bed Saint Francis Medical Center in Cape Girardeau, Mo., and Physicians Advanced Health Care Group, a 39-physician group practice. The campus would include a 50-bed hospital, an ambulatory surgery center and other facilities.

Steven Bjelich, president and chief executive officer of Saint Francis Healthcare, said no one should assume that the partnership will buy Three Rivers, but no one should rule out the possibility either. Bjelich said the partnership already has opened a diagnostic imaging center and will open an ambulatory surgery center in June. The partners haven't filed for certificate-of-need approval for the 50-bed hospital because the Missouri Legislature is considering whether to abolish its CON laws, a move Bjelich supports. "I've seen the success of competition in Cape Girardeau," he said.

As for cost-cutting, Fetter said the $100 million in savings will be the first of several phases. Up first will be cuts in discretionary spending, such as meetings and travel, where the company could do less or do it for less money, he said. Tenet also will search for ways to lower the costs of companywide business functions, he said.




*Source: Tenet Healthcare Corp.*

### Stock option change

Tenet also said it would begin counting employee stock options as an expense on its income statements. A handful of companies, including Bank One Corp., Coca-Cola Co. and Washington Post Co., have announced plans to expense employee stock options, but no major healthcare-services company has agreed to do so until now.

Jack Bovender Jr., chairman and CEO of HCA, said in August that the company was studying the practice. Prescott said HCA decided against making the change because it hasn't become an industry norm and "it's tough to come up with something that accountants really believe is a solid valuation of those options."

HCA would reconsider if the practice becomes more standard among publicly traded hospital companies, he said.

Stock-option expensing has been a hot topic in investor circles in the wake of corporate accounting scandals in recent years, with some believing that expensing the options would reduce the incentives to executives to run up a company's stock price with gimmicky accounting. Accounting rules require companies to disclose the impact that options expensing would have on earnings per share, but the disclosure is made in a footnote to annual financial statements.

In another accounting change, Tenet said it would switch its fiscal year to coincide with the calendar year. The company said the change also aligns its fiscal 2003 with its adoption of a less aggressive policy toward Medicare outlier payments. «

Modern Healthcare

*April 14, 2003*

# Barbakow exits as chairman

## *Leader will keep CEO title as Tenet Healthcare Corp. struggles to bring in new investors, send a message*

It's not just Tenet Healthcare Corp.'s hospital portfolio that's getting trimmed. Tenet's top executive is having his job portfolio cut in half, as part of an overhaul of the company's corporate governance that Tenet hopes will win back investors' confidence.

Chief Executive Officer Jeffrey Barbakow will relinquish his title as chairman and leave the Santa Barbara, Calif.-based company's board after the firm's next annual meeting, expected to be no later than October. Three other directors will step down with Barbakow; all four will be replaced by independent directors.

The message of change came as Tenet reported financial results that indicate the devastating effects that changes in its Medicare outlier reimbursements are having on earnings, leading to the company's first quarterly loss since the fourth quarter of its fiscal 1999. For the three months ended Feb. 28, Tenet lost $55 million, or 12 cents per share, compared with profits of $280 million, or 56 cents per share, in fiscal 2002's third quarter. Tenet said its Medicare outlier payments fell to $40 million for the quarter, vs. $191 million in the year-ago quarter.

**Barbakow to relinquish chairman position.**

The corporate governance changes are "in response to our shareholder concerns," Barbakow told investors and analysts during a conference call last week. "Our shareholders voiced the need to change the makeup of our board of directors." He added, "I'm not aware of any public companies in which the CEO is not a member of the board."

It's not clear if Barbakow's situation will be unique, but it is definitely rare for a CEO to be excluded from his company's board, said Cheryl Gustitus, vice president of communications for Institutional Shareholder Services, Rockville, Md., which provides advice on proxy statements and corporate governance.

ISS strongly supports splitting the jobs of chairman and CEO, Gustitus said. "We want to see the chairman run the board and the CEO run the company," she said. Allowing one person to serve as chairman and CEO diminishes the board's ability to oversee management and gives the CEO too much control of the board's deliberations, she added. Estimates of the percentage of U.S. companies that combine the chairman and CEO posts run as high as 80%.

Tenet's series of corporate governance changes follows a string of other restructuring moves that Tenet has announced in recent months as the company has sought to deal with the fallout from its high Medicare outlier payments. Since the uproar about the size of its outlier payments, Tenet has become the target of investigations regarding the outlier payments, antitrust issues and physician matters at two of its California hospitals. The restructuring moves include overhauling management, cutting its divisions to two from three and announcing plans to sell or close 14 hospitals.

Darren Lehrich, a healthcare stock analyst with SunTrust Robinson Humphrey, said Tenet is listening to "strong, passionate input from shareholders" that the company's board needs to be more independent of management. The message is especially resonant because of the serious turmoil at HealthSouth Corp., Birmingham, Ala., which last week also announced measures to make its board more independent, he said. (See related story, p. 6)

As for Tenet's earnings, Lehrich said the dramatic reversal of fortune was no surprise. What will be important to watch is how the company fares as it renegotiates managed-care contracts this year, he added.

Not all of Tenet's major shareholders have been placated. Tom Timey, an analyst with American Century Investments, Kansas City, Mo., opened the question-and-answer session of the conference call by caustically congratulating Barbakow for keeping his job, saying it was "a remarkable achievement" for the CEO.

Another shareholder, M. Lee Pearce, also stepped up his criticism of management last week. Pearce has had several dust-ups with Tenet and its predecessor companies. In a news release, he alleged that Tenet could face a liability of up to $6 billion from investigations into its Medicare outlier payments. Also, posted on the Web site for Pearce's self-appointed Tenet Shareholder Committee is an April 7 letter to Tom Scully, administrator of the Centers for Medicare and Medicaid Services, in which Pearce called on the federal government to prosecute Tenet under the False Claims Act, and other civil fraud and criminal laws.

Tenet isn't taking Pearce's criticism lying down. The company filed a securities lawsuit against him in U.S. District Court in Los Angeles last week, accusing him of waging a proxy fight to change the company's board without making the proper filings to do so with the Securities and Exchange Commission. Tenet's complaint said that Pearce's news release fails to disclose "the lack of a reasonable basis" for Pearce's liability claims. Tenet asked the court to issue a preliminary injunction ordering him to follow the proxy provisions of federal securities laws and "to cease making false and misleading statements regarding Tenet."

Gary Cripe, a lawyer for Pearce and the committee, said through a spokesman that he is reviewing the suit, but after an initial reading, "it appears to be without merit."

Despite the furor, Barbakow tried to remain upbeat during last week's conference call. "The core business is solid," he said. "The right management is in place, and we're committed to doing whatever it takes." «

The New York Times

THURSDAY, JULY 10, 2003

# Tenet Healthcare Says U.S. Inquiry Is Intensifying

By ANDREW POLLACK

LOS ANGELES, July 9 — Tenet Healthcare said today that it was being formally investigated by the Securities and Exchange Commission, adding to a growing list of investigations and lawsuits the company is facing.

Tenet, the nation's second-largest profit-making hospital chain, said it received a subpoena on Tuesday for documents going back to May 31, 1997, related to certain payments from Medicare and insurance companies as well as to the company's financial disclosures.

Tenet's stock has dropped steeply since last fall, when it said that much of its rapid profit growth in the last couple of years came from "outlier" payments, which Medicare makes for treatment of especially costly cases. Those payments, and similar ones from private insurers known as stop-loss payments, rose rapidly after Tenet hospitals began sharply increasing their list prices in 1999.

Based on Tenet's description of the subpoena, the S.E.C. is apparently looking at whether Tenet executives misled investors by not informing them well enough that the company's growth was closely tied to those payments, which some analysts have characterized as a Medicare loophole.

Tenet said in November that the S.E.C. was informally looking into the outlier payments and also into trading of the company's stock before the news of its dependence on outlier payments broke in October.

But the issuance of the subpoena indicates the investigation has become a formal one, which is more serious. An informal investigation can be initiated by a regional office of the S.E.C. and does not give the agency the power to subpoena

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documents or testimony. A formal one must be approved by the commission in Washington and carries subpoena power.

Tenet, based in Santa Barbara, Calif., said in a statement that it would cooperate with the S.E.C., as it has been doing. A spokeswoman in the S.E.C. office in Los Angeles, which sent the subpoena to Tenet, declined to comment.

Tenet is already under investigation by the Justice Department over its outlier payments and also for other possible violations of Medicare regulations. Its hospital in Redding, Calif., was raided last fall after allegations were made that two heart doctors there performed unnecessary procedures on hundreds of patients. The chief executive of Tenet's Alvarado Hospital Medical Center in San Diego was indicted last month on charges of making illegal payments to doctors to induce them to refer patients to the hospital. In general, Tenet has denied wrongdoing. The Alvarado chief executive, Barry Weinbaum, has also denied the charges.

The company is also facing numerous lawsuits from shareholders saying the company misled them about earnings — there were 20 such suits filed just from November to January — as well as lawsuits from patients in Redding claiming mistreatment by the heart doctors there.

Given all the other problems, investors seemed to take the S.E.C. news in stride. Tenet's shares fell only 5 cents today, to $12.10, though they have lost three-quarters of their value since fall.

"This thing is so multitudinous it's hard to know where the next asteroid is coming from," said John W. Ransom, an analyst at Raymond James & Associates. "You know that every three weeks or so, something like this is going to happen."

Mr. Ransom said the main impact of the S.E.C. investigation could be to help the plaintiffs in the private shareholder lawsuits. "Any evidence churned up about what people knew and when they knew it is going to raise the bar for such damages," he said. He also said the company might face a hefty fine.

***A focus seems to be what investors were told about dealings with Medicare.***

Any more fines and litigation costs would come as Tenet's earnings are falling sharply, not only because of the loss of outlier payments but because private insurers are bargaining for better terms and because costs are rising. Analysts said that Tenet's free cash flow, after capital expenses, was close to vanishing.

"They are getting deeper in the hole," Sheryl Skolnick, an analyst at Fulcrum Global Partners, said recently. "You can begin to see where the strength of the balance sheet deteriorates."

Tenet has already said it will sell or close 14 of its 114 hospitals to raise cash and is cutting capital expenditures to $700 million annually from $1 billion. But analysts say the company might have to make further cuts or sell even more hospitals, which would hurt its earnings in the long run.

The company still has an uptapped $1.5 billion line of credit and said it was not in danger of violating any loan covenants. Still, Moody's Investors Service cut the company's debt rating to junk status last month, saying that while it was not concerned about near-term compliance with financial covenants, it was concerned about compliance in the future.

Tenet also continues to face labor problems. Today, several nurses at its Centinela Hospital Medical Center in Inglewood, Calif., held a news conference outside the hospital gates to complain that the nursery and the neonatal intensive-care unit were understaffed, in violation of state regulations.

"It's potentially dangerous for you to deliver a child here," said Sara Davenport, a nurse in the neonatal care unit. She and other nurses said they had complained to the hospital's management, to no avail. The nurses said the situation has been like that for about two years and has not worsened noticeably in the last few months as Tenet's earnings have deteriorated.

The news conference was organized by the California Nurses Association, which is trying to unionize the nurses at Centinela and other Tenet hospitals in the state. Tenet, in hopes of achieving labor peace, reached an agreement in May with two other unions to represent workers in its hospitals. But the nurses association opposes that agreement and wants to represent the nurses.

Harry Anderson, a spokesman for Tenet, denied that staffing was inadequate, saying the charge was part of the union's effort to use "every means at hand in an effort to advance their organizing effort in a very competitive environment."